



AVATAR, INC.

FINANCIAL STATEMENTS
with
Independent Auditors' Report

Years Ended June 30, 2006 and 2005

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CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Avatar, Inc.
Ogden, Utah

We have audited the accompanying statements of financial position of Avatar, Inc. (a non-profit organization) as of June 30, 2006 and 2005, and the related statements of activities, functional expenses, and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Avatar, Inc. as of June 30, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 5, 2007 on our consideration of Avatar, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants for the year ended June 30, 2006. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Carver Hovey & Florek, LLC

January 5, 2007

AVATAR, INC.
STATEMENTS OF FINANCIAL POSITION
Years Ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 36,195	\$ -
Assets limited as to use (notes 1 and 2)	2,818	9,854
Accounts receivable	276,903	222,942
Employee loans	1,957	-
Total current assets	317,873	232,796
Property & equipment (net) (note 3)	850,971	707,675
Assets limited as to use (notes 1 and 2)	25,000	25,000
Deposits	-	1,950
Prepaid expenses	44,988	19,270
Intangible assets (net) (note 4)	18,611	16,772
	<u>\$ 1,257,443</u>	<u>\$ 1,003,463</u>
LIABILITIES AND NET ASSETS		
Current liabilities:		
Checks drawn in excess of cash	\$ 45,450	\$ 5,255
Accounts payable	142,630	62,848
Accrued interest	3,336	3,910
Accrued expenses	149,365	136,574
Capital lease	1,410	-
Loans payable to officer (note 8)	77,956	20,631
Current maturities of long-term debt (note 5)	46,402	26,385
Total current liabilities	466,549	255,603
Long-term debt, less current maturities (note 5)	778,184	590,756
Net assets:		
Unrestricted	(15,108)	122,250
Temporarily restricted	27,818	34,854
	<u>12,710</u>	<u>157,104</u>
	<u>\$ 1,257,443</u>	<u>\$ 1,003,463</u>

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENTS OF ACTIVITIES
Years Ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
UNRESTRICTED NET ASSETS		
Unrestricted revenues:		
Public support contracts	\$ 2,841,977	\$ 2,426,823
Client fees and other	174,984	158,724
Net assets released from restrictions:		
Restrictions satisfied by payments	<u>27,300</u>	<u>25,004</u>
Total unrestricted public support and revenue	3,044,261	2,610,551
Expenses:		
Group homes	2,340,999	1,953,703
Family support	155,116	173,256
Supported employment	179,551	92,382
Management and general	<u>485,689</u>	<u>352,283</u>
Total expenses	3,161,355	2,571,624
Net assets reclassified as temporarily restricted	<u>20,264</u>	<u>23,200</u>
Total expenses and restrictions	<u>3,181,619</u>	<u>2,594,824</u>
Increase (decrease) in unrestricted net assets	(137,358)	15,727
TEMPORARILY RESTRICTED NET ASSETS		
Net assets reclassified as temporarily restricted	20,264	23,200
Net assets released from restrictions	<u>(27,300)</u>	<u>(25,004)</u>
Decrease in temporarily restricted assets	<u>(7,036)</u>	<u>(1,804)</u>
INCREASE (DECREASE) IN NET ASSETS	(144,394)	13,923
NET ASSETS AT BEGINNING OF YEAR	<u>157,104</u>	<u>143,181</u>
NET ASSETS AT END OF YEAR	<u><u>\$ 12,710</u></u>	<u><u>\$ 157,104</u></u>

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENT OF FUNCTIONAL EXPENSES
Year ended June 30, 2006

	Group Homes	Family Support	Supported Employment	Management and General	Company Total
Salaries and related expenses:					
Salaries	\$ 1,646,606	\$ 98,115	\$ 134,942	\$ 266,637	\$ 2,146,300
Payroll taxes	138,237	7,928	11,339	21,529	179,033
	<u>1,784,843</u>	<u>106,043</u>	<u>146,281</u>	<u>288,166</u>	<u>2,325,333</u>
Consultants and foster parents	28,368	25,295	-	23,402	77,065
Accounting and audit	-	-	-	24,634	24,634
Staff training	-	-	-	-	-
Mileage reimbursement	14,654	13,074	7,553	2,692	37,973
Vehicle lease	29,550	-	-	-	29,550
Vehicle repairs and supplies	25,045	59	7,485	4,965	37,554
Telephone	20,518	763	1,726	24,384	47,391
Postage	5	-	-	1,456	1,461
Rent / lease	57,997	2,936	-	24,108	85,041
Utilities	41,284	130	-	7,977	49,391
Building remodel and maintenance	36,457	267	646	9,812	47,182
Equipment and furniture purchase	-	-	-	-	-
Equipment lease	-	-	-	10,495	10,495
Equipment and furniture repair	1,100	-	-	298	1,398
Medical equipment and supplies	243	-	-	239	482
Program services	9,461	213	2,177	5,983	17,834
Activity costs	6,145	61	593	310	7,109
Food	79,471	771	345	3,282	83,869
Office supplies	2,270	110	-	13,359	15,739
Other supplies	2,752	194	69	2,634	5,649
Conference per diem	885	-	500	8,917	10,302
Books and subscriptions	-	195	-	2,925	3,120
Insurance expense	101,224	5,005	11,262	14,722	132,213
Licenses and permits	2,120	-	-	2,425	4,545
Miscellaneous expense	-	-	-	324	324
Interest	63,680	-	-	2,521	66,201
Depreciation	32,927	-	914	5,659	39,500
	<u>\$ 2,340,999</u>	<u>\$ 155,116</u>	<u>\$ 179,551</u>	<u>\$ 485,689</u>	<u>\$ 3,161,355</u>

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENT OF FUNCTIONAL EXPENSES
Year ended June 30, 2005

	Group Homes	Family Support	Supported Employment	Management and General	Company Total
Salaries and related expenses:					
Salaries	\$ 1,357,420	\$ 149,527	\$ 71,532	\$ 176,523	\$ 1,755,002
Payroll taxes	105,680	7,162	5,560	27,956	146,358
	<u>1,463,100</u>	<u>156,689</u>	<u>77,092</u>	<u>204,479</u>	<u>1,901,360</u>
Consultants and foster parents	78,140	440	356	12,253	91,189
Accounting and audit	-	-	-	16,790	16,790
Staff training	43,360	2,145	1,858	4,069	51,432
Mileage reimbursement	23,736	10,119	2,410	5,375	41,640
Vehicle lease	31,233	-	-	-	31,233
Vehicle repairs and supplies	10,228	-	3,154	389	13,771
Telephone	15,314	817	692	16,024	32,847
Postage	14	-	-	2,486	2,500
Rent / lease	45,575	-	-	28,800	74,375
Utilities	29,533	-	43	5,657	35,233
Building remodel and maintenance	25,099	-	145	6,909	32,153
Equipment and furniture purchase	5,291	-	-	(43)	5,248
Equipment and furniture repair	3,335	-	-	125	3,460
Medical equipment and supplies	(7)	-	-	-	(7)
Program services	3,085	15	16	4,133	7,249
Activity costs	5,258	82	5	482	5,827
Food	44,399	10	47	375	44,831
Office supplies	6,105	250	-	15,861	22,216
Other supplies	5,862	186	54	5,572	11,674
Conference per diem	311	-	-	7,658	7,969
Books and subscriptions	200	258	-	6,049	6,507
Insurance expense	45,176	1,995	5,573	3,589	56,333
Licenses and permits	4,910	250	219	851	6,230
Miscellaneous expense	334	-	-	251	585
Interest	37,414	-	-	-	37,414
Depreciation	26,698	-	718	4,149	31,565
	<u>\$ 1,953,703</u>	<u>\$ 173,256</u>	<u>\$ 92,382</u>	<u>\$ 352,283</u>	<u>\$ 2,571,624</u>
Total expenses					

See accompanying notes and accountants' report

AVATAR, INC.
STATEMENTS OF CASH FLOWS
Years Ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase (decrease) in net assets	\$ (144,394)	\$ 13,923
Adjustments to reconcile change in net assets to net cash provided by operating activities :		
Depreciation and amortization	40,633	25,765
Changes in operating assets and liabilities :		
Accounts receivable	(53,961)	(40,302)
Employee loans	(1,957)	-
Prepaid expense and deposits	(23,768)	(10,838)
Assets limited as to use	7,036	1,804
Accounts payable	79,782	(512)
Accrued expenses	12,217	23,062
Intangible assets	(2,972)	-
NET CASH PROVIDED BY (USED BY) OPERATING ACTIVITIES	(87,384)	12,902
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(182,796)	(44,882)
NET CASH USED BY INVESTING ACTIVITIES	(182,796)	(44,882)
CASH FLOWS FROM FINANCING ACTIVITIES		
New debt - short-term	57,325	20,631
New debt - long-term	236,616	-
Principal payments of long-term debt	(27,761)	(25,764)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	266,180	(5,133)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(4,000)	(37,113)
CASH AND CASH EQUIVALENTS (DEFICIT) AT BEGINNING OF YEAR	(5,255)	31,858
CASH AND CASH EQUIVALENTS (DEFICIT) AT END OF YEAR	<u>\$ (9,255)</u>	<u>\$ (5,255)</u>

See accompanying notes and accountants' report

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

Avatar, Inc. (the Organization) is a non-profit corporation organized under the Utah Nonprofit Corporation and Cooperative Association Act. The principal objective and purpose for which the company was formed, as stated in its articles of incorporation, is to provide quality habilitative and rehabilitative services to persons with handicapping conditions and disabilities in the State of Utah.

Basis of Accounting

The accounts of the Organization are maintained, and the financial statements are prepared on the accrual basis of accounting. Accordingly, revenues and gains are recognized when earned, and expenses and losses are recognized when incurred.

Basis of Presentation

In accordance with SFAS No. 117, Financial Statements of Not-for-Profit Organizations, the Organization reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Use of Estimates

The financial statements include estimates and assumptions made by management that affect the carrying amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Property and Equipment

Acquisitions of property and equipment in excess of \$1,000 are capitalized. Property and equipment are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets (3 to 30 years).

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

Revenue and expenses are recorded on the accrual basis. Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Concentration of Revenue Sources

Government contracts represent approximately 93% and 95% of the Organization's source of revenues in fiscal 2006 and 2005, respectively.

Income Taxes

The Organization is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. However, income from certain activities not directly related to the Organization's tax-exempt purpose is subject to taxation as unrelated business income.

Cash and Cash Equivalents

Cash and cash equivalents includes all monies in banks and highly liquid investments with maturity dates of less than three months. The carrying value of cash and cash equivalents approximates fair value because of the short maturities of those financial instruments.

Assets Limited as to Use

Assets deposited with a trustee under terms of the note indenture (note 2) are classified as assets limited as to use.

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

1. NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Unamortized Bond Costs

Costs incurred in connection with the issuance of the Clearfield City, UT/UARF, Series 1997 Tax Exempt Bonds are amortized over the term of the bonds using the effective-interest method.

Functional Allocation of Expenses

The costs of providing the various programs and activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

2. ASSETS LIMITED AS TO USE

The assets limited as to use are composed of the following:

	<u>2006</u>	<u>2005</u>
CURRENT:		
Cash in Money Market accounts, designated for the bond sinking fund	<u>\$ 2,818</u>	<u>\$ 9854</u>
NON-CURRENT:		
Debt Service Reserve fund	<u>\$ 25,000</u>	<u>\$ 25,000</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

3. PROPERTY AND EQUIPMENT

Property and equipment at June 30 consisted of the following:

	<u>2006</u>	<u>2005</u>
Land	\$ 192,000	\$ 162,000
Buildings	714,930	587,222
Furniture & equipment	164,074	159,842
Vehicles	<u>48,034</u>	<u>27,178</u>
	1,119,038	936,242
Accumulated depreciation	<u>(268,067)</u>	<u>(228,567)</u>
	<u>\$ 850,971</u>	<u>\$ 707,675</u>

4. INTANGIBLE ASSETS

Intangible assets at June 30 consisted of the following:

	<u>2006</u>	<u>2005</u>
Prepaid loan fees	\$ 11,117	\$ 8,145
Bond issuance fees	<u>14,265</u>	<u>14,265</u>
	25,382	22,410
Accumulated amortization	<u>(6,771)</u>	<u>(5,638)</u>
	<u>\$ 18,611</u>	<u>\$ 16,772</u>

The prepaid loan fees and bond issuance costs are amortized over 15 years.

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

5. NOTES PAYABLE

Notes payable as of June 30, 2006 and 2005 were as follows:

	<u>2006</u>	<u>2005</u>
Clearfield City, UT/UARF Mortgage Revenue Bonds, with interest at 7.70% due in increasing annual installments of \$5,000 in 1998 to \$25,000 in 2022, with interest due semi-annually, secured by real estate and the net rental revenue	\$ 245,000	\$ 250,000
Washington Mutual, with interest at 5.625% and monthly payments of \$922.58, maturing August, 2017, collateralized by real estate	92,174	97,897
Washington Mutual, with interest at 5.625% and monthly payments of \$996.72, maturing August, 2017, collateralized by real estate	98,674	104,839
Washington Mutual, with interest at 5.625% and monthly payments of \$762.78, maturing August, 2017, collateralized by real estate	75,724	81,280
Washington Mutual, with interest at 5.625% and monthly payments of \$787.49, maturing August, 2017, collateralized by real estate	79,039	83,125
Washington Mutual, with interest at 6% and monthly payments of \$806.70, maturing August, 2036, collateralized by real estate	133,318	-
Loan from a bank, with interest at 9.3% and monthly payments of \$1680.93, maturing June, 2011, guaranteed by the Executive Director	80,125	-
Loan from a credit union, with interest at 6.15% and monthly payments of \$406.53, maturing February, 2011, collateralized by a vehicle	<u>20,532</u>	<u>-</u>
Total	824,586	617,141
Less current maturities of long-term debt	<u>(46,402)</u>	<u>(26,385)</u>
Net long-term debt	<u>\$ 778,184</u>	<u>\$ 590,756</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

5. NOTES PAYABLE (Continued)

Notes payable mature as follows:

<u>Year Ended June 30</u>	<u>Amount</u>
2007	\$ 46,402
2008	54,410
2009	57,576
2010	60,980
2011	63,564
Thereafter	<u>541,654</u>
	<u>\$ 824,586</u>

Interest accrued on notes and mortgages as of June 30, 2006 and 2005 was \$3,336 and \$3,435, respectively.

6. COMMITMENTS

Operating Leases

Avatar, Inc. is obligated under operating leases for group homes, office space and certain equipment. Such leases are summarized below:

<u>Facility</u>	<u>Expiration Date</u>	<u>Annual Costs</u>
Apartments and homes	Various to June, 2009	\$ 60,933
Utah Office	April, 2007	25,200
Vehicles and Equipment	Various to June, 2010	<u>20,550</u>
		<u>\$ 115,683</u>

Operating Lease commitments for the next five years are as follows:

<u>Year Ended June 30</u>	<u>Amount</u>
2007	\$ 86,905
2008	39,600
2009	36,000
2010	10,800
2011	-
Thereafter	<u>-</u>
	<u>\$ 173,305</u>

AVATAR, INC.
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2006 and 2005

6. COMMITMENTS (Continued)

Rental expenses under operating leases for the years ended June 30, 2006 and 2005 were \$ 95,536 and \$74,375, respectively.

Insurance and maintenance expenses are generally obligations of the Company and accordingly are not included as part of the rental payments.

7. SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest totaled \$ 66,201 and \$33,504 for the years ended June 30, 2006 and 2005, respectively.

8. RELATED PARTY TRANSACTIONS

Avatar has a loan payable to an officer of \$77,956 and \$20,631 for the years ended June 30, 2006 and 2005. This loan has an interest rate of 7.50% and only interest has been paid on it of \$1,263 and \$475 for the years ended June 30, 2006 and 2005, respectively. The Executive Director has personally guaranteed the loan for \$80,125. See note 5.

Included in accounts receivable at June 30, 2006 is a receivable from a member of the Board of Trustees in the amount of \$4,967 for repairs on a rental property done by Avatar.

9. DEBT COVENANTS

The Clearfield City, UT/UARF mortgage revenue bonds, detailed in note 5, have restrictive loan covenants that require the Company to maintain various balances and ratios. The financial covenants are as follows;

Debt Service Coverage Ratio: 1.25
Long-term indebtedness
Short-term indebtedness
Liquidity: 30 days cash on hand at year-end
Trade Payables
Current Ratio: 1.25

As of June 30, 2006, the Company did not comply with any of the covenants.



CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Trustees of
Avatar, Inc.

We have audited the financial statements of Avatar, Inc. (a non-profit organization) as of and for the year ended June 30, 2006, and have issued our report thereon dated January 5, 2007. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Avatar, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Avatar, Inc.'s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information and use of the management of Avatar, Inc. and state and federal awarding agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Carver Hovey + Florek, LLC

January 5, 2007



CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

REPORT ON STATE LEGAL COMPLIANCE

To the Board of Trustees
Avatar, Inc.

We have audited the financial statements of Avatar, Inc. (a non-profit organization) as of and for the year ended June 30, 2006, and have issued our report thereon dated January 5, 2007. As part of our audit, we have audited Avatar, Inc.'s compliance with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; special tests and provisions applicable to its major State assistance program as required by the State of Utah Legal Compliance Audit Guide for the year ended June 30, 2006. Avatar, Inc. received the following major State assistance program from the state of Utah:

RESIDENTIAL

The management of Avatar, Inc. is responsible for its compliance with the compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about Avatar, Inc.'s compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed no instances of noncompliance with the requirements referred to above.

In our opinion, Avatar, Inc. complied, in all material respects, with the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; and special tests and provisions that are applicable to its major State assistance program for the year ended June 30, 2006.

Carver Hovey & Florek, LLC

January 5, 2007



CARVER HOVEY & FLOREK, LLC

CERTIFIED PUBLIC ACCOUNTANTS

STEVEN L. CARVER, CPA
KATHLEEN L. HOVEY, CPA
BRENT R. FLOREK, CPA

To the Board of Directors
Avatar, Inc.
Ogden, Utah

January 5, 2007

Ladies and Gentlemen:

We have audited the financial statements of Avatar, Inc. for the year ended June 30, 2006, and have issued our report thereon dated January 5, 2006. In planning and performing our audit of the financial statements of Avatar, we considered internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. An audit does not include examining the effectiveness of internal control and does not provide assurance on internal control.

Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control and its operation that we consider to be material weaknesses as defined above.

During our audit we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations are intended to improve internal control or result in other operating efficiencies and are summarized as follows:

Adhering to the Budget

We noted that several major areas of expense were over budget, namely personnel costs and insurance. We recommend an adequate budget for personnel costs be adopted and strictly adhered to. The budget is the Company's best measure and standard to keep it on course throughout the year. Financial performance should be compared to the budget regularly and variances explained. If revisions to the budget are warranted they should be made and a new budget adopted for the remaining part of the year.

Loan covenants

The covenants on the Zions Bank mortgage require various balances and ratios to maintain compliance with the covenants. Also this information is required to be reported quarterly. As

of June 30, 2006 the Company was in default on three major covenants and had not been timely in reporting to Zions on their quarterly reports.

We have prepared the annual report to Zions as required. The Bank will respond after they receive the report. We recommend the Company follow any recommendations the bank has.

Employee and Director loans

The Company made loans to employees and are having them repay them monthly. If it is at all possible we do not recommend doing this.

The Company also incurred almost \$5,000 in materials and labor doing repairs on a property owned by a member of the Board which was still outstanding months later. We recommend this bill be immediately collected and the practice prohibited in the future.

Reconciling items on the bank statement

We noted that there were a number of outstanding checks on the bank reconciliation that were very old. We recommend that these items be researched and dealt with now.

We noted no other reportable or significant matters during our testwork.

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This report is intended solely for the information and use of the audit committee, management, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

Camm Hovey & Flook, LLC